SERRALA

Best Practices in AR

**Best Practices in Accounts
Receivable Processing:
Automating Cash Application**

01

Introduction

For companies seeking to improve the order-to-cash cycle in finance, cash application is a good place to start. By automating this process, companies can tap into a number of benefits. However, in practice levels of automation can vary considerably – so companies should understand the factors which can impede automation, as well as the best practices which can produce the greatest efficiencies.

Accounts receivable is crucial to the success of any business. Getting paid by customers in a timely and efficient way is essential if companies are to manage cash flows effectively, minimise days sales outstanding (DSO) and reduce portfolio risks. However, this is also an area which can present considerable challenges, from automating manual processes to overcoming variations in local practices.

In order to manage accounts receivable as effectively as possible, companies need to have efficient processes in place across the entire order-to-cash cycle in finance. The order-to-cash cycle incorporates all of the business processes involved in customer sales, from receiving an order to receiving payment:

- **Credit management** – evaluating customers, defining payment conditions and monitoring credit utilisation.

- **Invoice management** – sending invoices to customers and ensuring that payment terms are correctly displayed.

- **Dispute management** – handling and assigning disputes and managing escalation levels depending on case priority.

- **Collecting payment** – collecting funds, managing the dunning process and prioritising different collection cases as appropriate.

- **Cash application** – allocating the payment received against the open items in the company's ERP system.

Each of these process areas has its own challenges and priorities, and a robust order-to-cash cycle in finance requires efficiencies in all of these areas. However, this paper will focus on one specific area where companies can make considerable improvements: the cash application process.

02

Goals and objectives

As noted above, cash application is the process of matching payment information against open items. Within this area, companies typically have a number of specific goals:

- **Speed.** A key goal is to apply payments as soon as possible, thereby reducing DSO and enabling the company to use the cash at the earliest opportunity.

- **Accuracy.** While speed is important in the cash application process, it is also essential that cash is applied correctly. Incorrect application of cash can lead to negative customer feedback, as well as delaying the initiation of the dunning process. In order to apply cash accurately, companies need to have robust processes in place to collect the relevant information from customers.

- **Standardisation.** A further goal is standardisation and harmonisation. For international organisations, different country-specific processes and payment types can make it challenging to apply cash consistently across the organisation. By ensuring that the process is as harmonised as possible across different markets, companies can increase efficiency and reduce compliance challenges.

Companies may aspire to fast, accurate and standardised cash application processes. But in practice, this is an area which can present considerable challenges, not least because cash application includes highly manual processes, such as checking invoice numbers and amounts against open items.

In order to reduce the time spent on these repetitive tasks, many companies take the decision to automate their cash application processes by adopting a suitable IT system. Typically companies will be looking for an easy-to-implement solution which will have minimal impact on the company's existing ERP system. They will also look for a system which will reduce the time spent on cash application and deliver efficiency gains.

> While some organisations achieve levels of cash application auto-mation of over 90%, this can be as little as 40-60% for other companies, meaning that the benefits of the exercise are somewhat limited.

These goals can certainly be achieved – but in practice, some companies are able to automate the cash application process more successfully than others.

03 Challenges

There are a number of reasons why companies may struggle to achieve a higher level of process automation. These include the following:

Technology limitations

In some cases, the automation possibilities within the company's existing ERP system or sub ledger system may be limited. SAP, for example, provides a basic functionality for processing electronic bank statements, which works well and can be significantly enhanced with specialised solutions building on this functionality to deliver even higher automatic matching rates.

Diverse payment instruments

The effectiveness of cash application automation will be affected by the payment instruments used by the company's customers. The highest levels of automation can usually be achieved with direct debits, but companies may also support other instruments such as cheque payments, electronic transfers and PayPal.

This can be a particular challenge for companies operating internationally, which may need to process diverse sources of information. In the US, for example, there is a greater focus on the lockbox / cheque processing.

In contrast, companies operating in Europe are typically able to access the necessary information from bank statements and payment advices.

Diverse formats (bank statements, remittance advices, et al.)

Different banks may provide information in diverse formats, all of which will have to be handled in the company's IT environment. In practice, the IT system may not always be able to handle all of the relevant formats.

The automation process can become even more complex when companies receive separate payment information and remittance advice from customers. This information may be sent in a variety of different formats: Excel, PDF, Word documents, email and even paper remittance advices are all common. Converting all of this information into a standard format that can be processed by the company's IT solution takes time.

Transparency

Achieving transparency over the automation process can be a further challenge. Not all companies monitor their automation rates, and many do not know how many payments are being processed manually. These are key indicators which should be analysed in order to understand how efficient the current processes are and where opportunities for improvement can be found.

IT attention

In addition, getting the time and support from IT can present some challenges. Automating the cash application process usually requires communication with IT as well as with other relevant departments.

04

Best Practice

Assess your status quo

In order to overcome these challenges and achieve the highest possible level of automation, companies should first undertake a detailed evaluation of the current cash application process and any specific pain points. Each organisation will face its own obstacles in this area, so best practice will vary from company to company depending on various factors, such as geographical footprint and banking relationships.

Consult experts for best solutions

Once companies have achieved a clear picture of the current state, the next step should be to identify any external expertise which will be needed for the project. This should involve consulting experts who have extensive experience of delivering cash application projects with different clients. Experts should be able to advise what level of automation is achievable and which steps will need to be taken in order to achieve it. They can also help with the initial analysis of the status quo and provide support in selecting any IT resources required to achieve the highest possible automation rate.

Configurable technology to cope with different formats and payment instruments

Where the desired solution is concerned, best practice is to have a solution in place which is flexible enough to handle any format, from PDF to paper, and to collect the relevant information and make it available in the company's ERP system. Users of the system should not need to ask different colleagues where various payment advices are located, but instead should be able to find them directly in the system and linked to the respective payments.

Companies with an international scope should select a global solution which can handle all of the challenges, rather than having different country specific solutions in place.

Self-learning/Machine-learning for further automation

Best practices in this area also includes linking the payment advice with the bank statement item. In addition, companies should ensure that as soon as a remittance advice is received, it should be recognised in the IT environment and processed automatically in order to achieve straight through processing.

Self-learning features in the area of robotic process automation including intelligent algorithms that help reconcile open items, for example, based on previous customer data or sending bank details which enable even higher automation rates. With the introduction of powerful ERP infrastructures like S/4HANA it is even possible to further push the limits of real-time big data analysis to enable a more automated finance process.

Business driven approach

Solutions that empower the key user in the finance department to shape the system to the company's individual needs support an approach that is driven by business needs rather than technical concerns. With the finance department in a position to configure, adapt and design new algorithms themselves they can be more independent from IT and they have the possibility drive further efficiency gains.

05

Benefits

Achieving a high level of cash application automation can bring numerous benefits. Companies can reduce reconciliation issues, reduce DSO and initiate the dunning process sooner or trigger other following processes faster such as issuing travel documents to customer. As well as improving the cash application process itself, automation can also bring wider benefits for the order-to-cash cycle in finance.

For example, higher levels of automation can speed up the dispute process as the dispute management team can be informed more quickly if a payment cannot be applied. The credit management and invoice management processes can also be improved when cash application is automated.

As well as benefiting other parts of the order-to-cash cycle, companies may also be able to free up resources for other processes within accounts receivable.

06 The Journey Ahead

While many companies are already achieving high levels of automation in the area of cash application, further possibilities are emerging as technology continues to develop. Order-to-cash in finance is one area in which robotic process automation can play a role – particularly for companies which allow customers to pay using many diverse payment instruments. Cash application includes repetitive actions, such as matching invoice numbers against open items, which have plenty of scope to be improved with robotic process automation.

Meanwhile, companies which have implemented shared service centres may have opportunities to outsource their cash application process. Before doing so, companies should first review how best they can improve the area of cash application from both a technical and process perspective.

Looking forward, standardising and harmonising the cash application process will only become more relevant. It is important to understand that cash application is not a static process: this is a very dynamic area, with new payment methods and evolving payment behaviour presenting additional challenges. Companies are continuing to look for new opportunities to automate processes across the entire order-to-cash cycle in finance – and cash application is a good place to start as the return of investment for enhancement projects is high.

Serrala Brings Clarity to Complexity

Serrala optimizes the universe of payments for organizations that seek efficient cashvisibility and secure financial processes. Serrala supports over 3,500 companiesworldwide with advanced technology and personalized consulting to optimize all processes that manage incoming and outgoing payments: from order-to-cash, procure-to-pay and treasury to data and document management. Represented on three continents with 17 regional offices in Europe, North America, Middle East and Asia, over 600 employees are dedicated to service companies of all industry sectors — from medium-sized companies to global players. Over 30 years of industry experience provide us with the necessary knowledge and understanding to be your trustworthy partners.

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